No. 04-1264

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IN THE

Supreme Court of the United States

BUCKEYE CHECK CASHING, INC.,
Petitioner,

v.

JOHN CARDEGNA, *et al.*,
Respondents.

On Writ of Certiorari to the Supreme Court of Florida

BRIEF *AMICI CURIAE* OF THE NATIONAL ASSOCIATION OF CONSUMER ADVOCATES, THE U.S. PUBLIC INTEREST RESEARCH GROUP, AND THE CENTER FOR RESPONSIBLE LENDING IN SUPPORT OF RESPONDENTS

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INTEREST OF *AMICI CURIAE* [1]

The National Association of Consumer Advocates ("NACA") is a nationwide non-profit corporation whose over 1000 members are private and public sector attorneys, law professors, law students, and non-attorney consumer advo-

[1] A letter of consent from each of the parties has been filed with the Clerk of the Court. Although counsel for the respondents is an officer and a member of the National Association of Consumer Advocates, no counsel for a party authored this brief in whole or in part, and no person or entity other than *amici curiae* made a monetary contribution to the preparation or submission of this brief.

cates. NACA members' primary interest is the protection and representation of consumers. NACA's mission is to promote justice for all consumers and to provide a forum for information sharing among consumer advocates across the country. From its inception, NACA has focused on issues concerning abusive and fraudulent practices by businesses that provide financial and credit-related services.

NACA's members, as representatives of borrowers and other consumers across this nation, have witnessed first-hand the negative impact that pre-dispute, binding mandatory arbitration clauses have on the ability of average citizens to obtain justice. NACA is concerned that consumers will not be able to challenge illegal contracts effectively if the Florida Supreme Court's ruling is reversed.

The U.S. Public Interest Research Group ("U.S. PIRG") serves as the national advocacy office and association for state PIRGs, which are non-profit, non-partisan public interest advocacy organizations with over 500,000 members around the country. The state PIRGs and U.S. PIRG have a long history of advocacy on behalf of consumer rights in the financial and legal marketplace, and have produced numerous reports and studies documenting unfair practices of payday lenders, rent-to-own stores, and other predatory lenders. The PIRGs are also founding members of a national network of organizations seeking to ban the use of binding mandatory arbitration in consumer contracts.

The Center for Responsible Lending ("CRL") is dedicated to protecting home ownership and family wealth by working to eliminate abusive financial practices. A non-profit, non-partisan research and policy organization, CRL promotes responsible lending practices and access to fair terms of credit for low-wealth families. CRL's experience with lending issues is enhanced by its affiliation with Self-Help, one of the nation's largest community development financial institutions.

CRL is interested in this case because a victory for the petitioner would make it even more difficult for consumers to challenge illegal lending practices, such as the payday loan violations alleged in this case. CRL views illegal payday lending as both a consumer issue and a civil rights issue. Research by CRL has shown that payday loans trap borrowers in a cycle of debt and that North Carolina payday lending storefronts are disproportionately located in African-American neighborhoods. Uriah King et al., CRL, Race Matters: The Concentration of Payday Lenders in African-American Neighborhoods in North Carolina (2005), *available at* http://www.responsiblelending.org/pdfs/PaydayRace-Mar05.pdf; Keith Ernst et al., CRL, Quantifying the Economic Cost of Predatory Payday Lending 2 (2003), *available at* http://www.responsiblelending.org/pdfs/PaydayStudy-Dec03.pdf (finding that 91% of payday loans are made to borrowers with 5 or more payday loans per year and that borrowers, on average, receive 8 to 13 payday loans per year).

In addition to studying payday loans, CRL has worked on a number of other loan products affected by binding mandatory arbitration. Many lenders routinely insert binding mandatory arbitration clauses into contracts for mortgage loans, credit cards, refund anticipation loans, car title loans, and other products.

NACA, U.S. PIRG, and CRL share the concerns about the payday lending industry expressed by *amicus curiae* AARP and others. This separate brief is submitted to respond to assertions made by the petitioner and various *amici curiae* regarding binding mandatory arbitration and its effects on consumers.

SUMMARY OF ARGUMENT

Several *amici curiae* supporting the petitioner describe arbitration as an inexpensive and efficient method of resolving claims and assert that arbitration favors consumers. This

characterization is at odds with the reality experienced by consumers forced into binding mandatory arbitration.

If courts are prohibited from adjudicating the legality of contracts that contain mandatory arbitration clauses, arbitration costs will deter many consumers from challenging illegal contracts. Fees that can be high and unpredictable, unreliable fee waiver programs, inconvenient forum requirements, and consumers' inability to share costs combine to make arbitration much more expensive for many consumers than proceeding in court. Arbitration conducted pursuant to a typical mandatory arbitration clause also lacks many of the natural efficiencies that our judicial system derives from its class action rules, transparency, and reliance on precedent. The ways in which arbitral proceedings expedite claims, such as not requiring a statement of the arbitrator's reasoning, do not result in real efficiency, but instead make it even more important that courts rather than arbitrators decide whether contracts are illegal or unenforceable under state law.

Far from favoring consumers, binding mandatory arbitration makes it extremely difficult for consumers to challenge illegal contracts for a number of reasons, including stringent secrecy requirements, prohibitions on class actions, and limits on discovery and available remedies. Companies may also benefit as repeat players in arbitration proceedings. These aspects of arbitration deter many consumers from filing and make it difficult for those who do pursue claims to prevail. The study by Ernst & Young LLP that several *amici curiae* cite to support their argument that arbitration favors consumers suffers from serious deficiencies, including the use of flawed measures to determine when consumers prevailed and the very small number of responses Ernst & Young received to its phone survey. Because so many obstacles prevent successful challenges to illegal contracts in binding mandatory arbitration proceedings, consumers should have access to the courts to bring such challenges.

In response to concerns that arbitrators will enforce illegal contracts, the petitioner and Financial Service Centers of America, Inc. ("FiSCA") allude to post-arbitration judicial review and police powers respectively. These lines of argument fail to acknowledge how difficult it is under current law to vacate an arbitral decision and the critical role that Congress and state legislatures intend private enforcement to play in enforcing consumer protection laws.

ARGUMENT

I. ARBITRATION COSTS WILL PREVENT MANY CONSUMERS FROM CHALLENGING ILLEGAL CONTRACTS IF THE PETITIONER PREVAILS.

The American Bankers Association, the Community Financial Services Association of America ("CFSA"), and FiSCA characterize arbitration in their *amicus curiae* briefs as an inexpensive way to resolve claims. (American Bankers Association Br. 1-2; CFSA Br. 2; FiSCA Br. 6.) In fact, arbitration costs can be vastly higher for some consumers than the costs of filing a court action because of large fees, discretion associated with fee waiver programs, requirements that arbitration take place in a distant forum, consumers' inability to share costs through class actions, and the practical difficulty of challenging arbitration costs in court.

While arbitration companies have imposed caps on fees that consumers must pay in some arbitration proceedings, the caps often have significant exceptions. For example, the American Arbitration Association ("AAA") retains the "discretion to apply or not to apply" the provisions of its Supplementary Procedures for Consumer-Related Disputes, which include its maximums on consumer fees for consumer claims. AAA, Supplementary Procedures for Consumer-Related Disputes (2005), *available at* http://www.adr.org/sp.asp?id=22014. These maximums also do not apply to claims

for more than $75,000 or claims seeking non-monetary relief, such as injunctions, which are often important in consumer protection actions. *Id.* (setting a cap on the consumer portion of the arbitrator's fees at $125 for claims less than $10,000 and at $375 for claims between $10,000 and $75,000). Consumers with larger claims or non-monetary claims must pay administrative fees based on AAA's much more expensive commercial schedule and must deposit half of the arbitrator's compensation in advance. *Id.*; AAA, Commercial Arbitration Rules and Mediation Procedures (2005), *available at* http://www.adr.org/sp.asp?id=22002 (starting fees at a $1,800 initial filing fee plus a $750 case service fee for commercial claims between $75,000 and $150,000 and requiring a $3,250 initial filing fee and a $1,250 case service fee for non-monetary claims).

Like AAA, the National Arbitration Forum ("NAF") charges consumers higher fees for larger claims, a practice that may discourage consumers from claiming the full amount of their loss. NAF, Fee Schedule 9-13 (2005), *available at* http://www.arb-forum.com/programs/code_new/2005_fees.pdf. Although NAF caps filing and participatory hearing fees for smaller claims at $250, these caps do not apply if the claim exceeds $74,999 or if the parties have agreed otherwise. *Id.* at 4, 9-13. Above and beyond the filing and participatory hearing charges, NAF imposes additional fees as the arbitral proceedings progress, such as fees to process objections or to file a post-hearing memorandum, making it very difficult to predict the total cost of arbitration. *Id.* at 5-13 (describing several types of fees and stating that "[t]he Forum establishes all other fees").[2]

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[2] Even if an arbitration provider has a cap on fees that protects consumers from the high costs of arbitration at the time of filing, it may nevertheless permit the infliction of excessive costs on consumers who do not prevail. For example, while consumers who arbitrate through JAMS are required to pay only $125 if they initiate arbitration, a consumer who

Some arbitration providers charge a separate, significant fee for the arbitrator's time, an additional expense that has no parallel in the court system. Since arbitrators who work for the same arbitration provider can charge different rates, consumers subject to such charges may have to pay initial filing fees just to learn what the hourly rate will be for the arbitrator who may hear their claim. *See Ting v. AT&T*, 182 F. Supp. 2d 902, 916-17 (N.D. Ca. 2002), *aff'd in relevant part, rev'd in part*, 319 F.3d 1126 (9th Cir.), *cert. denied*, 540 U.S. 811 (2003). In a random sampling of AAA commercial arbitrators in northern California, the average arbitrator compensation ranged from $600 to $3,850 per day. *Id.* at 917; *see also Phillips v. Assocs. Home Equity Servs., Inc.*, 179 F. Supp. 2d 840, 846 (N.D. Ill. 2001) (noting arbitrator fees ranging from $750 to $5,000 per day). A 2004 study by the California Dispute Resolution Institute considered fee data from over 1,400 arbitration cases and determined the average total arbitrator fee was $2,256. California Dispute Resolution Institute, Consumer and Employment Arbitration in California: A Review of Website Data Posted Pursuant to Section 1281.96 of the Code of Civil Procedure 21 (2004), *available at* http://www.mediate.com/cdri/cdri_print_Aug_6.pdf. The possibility of incurring all or part of such a large expense may deter consumers from filing claims, especially when payment is required in advance.[3]

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does not prevail in a JAMS arbitration may be required to pay the fees and costs incurred by the opposing party unless protected by California law. JAMS, Policy on Consumer Arbitrations Pursuant to Pre-Dispute Clauses Minimum Standards of Procedural Fairness (2005), *available at* http://www.jamsadr.com/rules/consumer_min_std.asp.

[3] While there are arbitrators who work *pro bono*, such services are typically limited in scope and availability. *See, e.g.*, AAA, Administrative Fee Waivers and Pro Bono Arbitrators Services (2003), *available at* http://www.adr.org/sp.asp?id=22040 (indicating that *pro bono* arbitrator services may be requested for one-day hearings, but are not guaranteed).

A 2002 study by Public Citizen of the three largest arbitration providers found that arbitration forum costs could be up to five thousand percent higher than court fees. Public Citizen, The Costs of Arbitration 2, 43 (2002), *available at* http://www.citizen.org/documents/ACF110A.PDF. The study also found vastly higher arbitration costs for certain types of claims brought under a pre-dispute clause than for similar claims submitted on a post-dispute basis. *Id.* at 2, 71. The study noted that there is little incentive for arbitration companies to cut costs for claims arbitrated pursuant to a pre-dispute clause, as opposed to a post-dispute arbitration agreement, because companies that insert pre-dispute clauses into their contracts want to limit the number of claims filed. *Id.* at 2.

Despite reductions in certain arbitration fees since 2002, the concerns expressed in the Public Citizen report remain for many consumers. The table below compares the cost that a consumer might face in arbitrating an $80,000 claim through a three-hour NAF participatory hearing to the cost of litigating the same claim in federal court.

Arbitration versus Court:
Sample Costs for $80,000 Consumer Claim

Item	Arbitration	Court
Filing fee	$300	$250
Commencement fee	$300	$0
Administrative fee	$1,000	$0
Requests for a subpoena, a discovery order, and an amendment	$675	$0
Participatory hearing (3 hours)	$1,500	$0
Post-hearing memorandum	$100	$0
Written findings of fact, conclusions of law, or reasons for award	$1,500	$0
Request for a dispositive order	$500	$0
Total	**$5,875**	**$250**

See NAF, Fee Schedule, *supra*, at 9-13; 28 U.S.C. § 1914.

Although many arbitration providers have fee waiver programs, these programs can be discretionary and unpredictable. For example, even if a consumer provides required financial information and meets AAA's indigency requirement, AAA reserves the right to deny a waiver. *See* AAA, Administrative Fee Waivers and Pro Bono Arbitrators Services (2003), *available at* http://www.adr.org/sp.asp?id=22040. Fee waivers also may not be available for all types of claims and may not cover some arbitration expenses. NAF, for instance, only permits waivers for claims of less than $75,000 and does not waive the fees that it charges for written findings of fact, conclusions of law, or reasons for the award. *See* NAF, Code of Procedure 2, 40 (2005), *available at* http://www.arb-forum.com/programs/code_new/2005_code.pdf; Mark E. Budnitz, *The High Cost of Mandatory Consumer Arbitration*, 67 Law & Contemp. Probs. 133, 144 (2004).

Clauses that require arbitrations to take place in a distant forum can further increase the costs for consumers. Many binding mandatory arbitration clauses include a provision specifying a particular location where the arbitration hearing must be held, which, if enforced, may result in significant travel expenses that would not be necessary to litigate a case in court. *See* Budnitz, *The High Cost of Mandatory Consumer Arbitration*, *supra*, at 149-50.

These expenses are particularly burdensome because of restrictions on class actions and joinder in arbitration proceedings. Class actions and consolidation of claims permit consumers to leverage resources to litigate claims that would otherwise be cost prohibitive. As the Court has recognized:

> "The policy at the very core of the class action mechanism is to overcome the problem that small recoveries do not provide the incentive for any individual to bring a solo action prosecuting his or her rights. A class action solves this problem by aggregating the relatively paltry

> potential recoveries into something worth someone's (usually an attorney's) labor."

AmChem Prods., Inc. v. Windsor, 521 U.S. 591, 617 (1997) (quoting *Mace v. Van Ru Credit Corp.*, 109 F.3d 338, 344 (7th Cir. 1997)); *see also Deposit Guar. Nat'l Bank v. Roper*, 445 U.S. 326, 338-39 (1980); *Ting v. AT&T*, 182 F. Supp. 2d at 930-31. Many consumer arbitration clauses specifically prohibit consolidation of claims or class actions, and even where an arbitration clause is silent, class actions are often not permitted. Budnitz, *The High Cost of Mandatory Consumer Arbitration*, *supra*, at 142-43, 149. Without the ability to proceed as a class, consumers cannot share expenses and may not be able to obtain necessary legal representation.[4]

Consumers who cannot afford arbitration and its associated expenses face an uphill battle to challenge arbitration costs in court. The onus is on the consumer to show the likelihood of incurring costs that are prohibitively expensive. *Green Tree Fin. Corp. v. Randolph*, 531 U.S. 79, 92 (2000). Given the uncertainties about what the fees will be and the lack of clarity regarding when expenses are considered prohibitive, many consumers are unable to make such a showing and abandon their claims. Budnitz, *The High Cost of Mandatory Consumer Arbitration*, *supra*, at 150-56. If the Court rules that consumers cannot challenge illegal contracts as void *ab initio* in court, the costs associated with arbitration and the

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[4] While FiSCA asserts that "[i]nformal consumer arbitration procedures do not require representation of a respondent business by lawyers" (FiSCA Br. 15), a recent California Dispute Resolute Institute survey suggests that consumers generally do require representation when they are parties to arbitration. In 79% of the 2,175 arbitration cases studied, the consumer party retained legal counsel. California Dispute Resolution Institute, *supra*, at 26. This is not surprising given the complex legal questions often present in consumer matters and the mismatch in sophistication between the business and the typical consumer in such arbitrations.

practical difficulty of challenging those costs may prevent many consumers from disputing such contracts at all.

II. ARBITRATION IS NOT AN EFFICIENT WAY TO RESOLVE CLAIMS THAT CONTRACTS ARE ILLEGAL.

The American Bankers Association states that upholding the decision of the Florida Supreme Court would "divert numerous disputes into the more expensive and less efficient court system." (American Bankers Association Br. 2.) According to CFSA, "[g]iven the small amount of a payday advance, arbitration is particularly well-suited to resolve disputes." (CFSA Br. 9.) Binding mandatory arbitration, however, actually creates many of the inefficiencies that these organizations claim to fear, especially when the issue in question is the legality of a form contract used in thousands of transactions. Arbitration proceedings conducted under a typical mandatory arbitration clause lack many of the natural efficiencies of the judicial system, including the economy of aggregating class-wide claims and the benefits of transparency and precedent.

The notion that companies favor arbitration for efficiency reasons is belied by the restrictions on class-wide arbitrations described above. This refusal to address like claims together is the antithesis of efficiency and prevents consumers from using their claims to obtain relief for all victims of a particular violation at once. *See Am. Pipe & Const. Co. v. Utah*, 414 U.S. 538, 553 (1974) (recognizing "efficiency and economy of litigation" as "a principal purpose of the [class action] procedure").

Another inefficiency of arbitration is the fact that arbitrators must resolve the same issues again and again as if for the first time, without making any contribution to the development of the law. In marked contrast to our open court system, secrecy shrouds the arbitral process. As Judge Diane P. Wood explained in an article in 2003, "[e]verything, from the

content of the demand for arbitration, through the materials submitted before the hearing, the hearing, and the ultimate reasons for the disposition, can be, and often is, maintained in absolute confidence." Diane P. Wood, *The Brave New World of Arbitration*, 31 Cap. U. L. Rev. 383, 397 (2003). Arbitrators are often not required to produce findings of fact or conclusions of law, and even the parties may not be privy to the reasoning behind an arbitrator's decision. *See, e.g., United Steelworkers of Am. v. Enter. Wheel & Car Corp.*, 363 U.S. 593, 598 (1960) ("Arbitrators have no obligation to the court to give their reasons for an award."); AAA, Commercial Arbitration Rules and Mediation Procedures, *supra*, at § R-42(b) ("The arbitrator need not render a reasoned award unless the parties request such an award in writing prior to appointment of the arbitrator or unless the arbitrator determines that a reasoned award is appropriate."). Moreover, "arbitrators' decisions are not intended to have precedential effect even in arbitration (unless given that effect by contract)." *IDS Life Ins. Co. v. SunAmerica Life Ins. Co.*, 136 F.3d 537, 543 (7th Cir. 1998) (citing cases). As a result, arbitrators are unable to build upon or benefit from prior arbitral decisions or reasoning.

To the extent that arbitration does expedite individual claims, it is primarily because arbitration denies participants necessary discovery and other litigation process that consumers require to develop their claims. For example, as Judge Wood explained in her article, "the arbitral rules used often place strict limits on document discovery, the number of depositions that will be permitted, and the matters that may be explored." Wood, *supra*, at 397. The so-called "efficiency" of this stripped-down procedure is not the way to resolve a claim that a contract is illegal under state or federal law.[5]

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[5] The American Bankers Association's assertion that a trip to the courthouse to determine the legality of a contract would render the arbitra-

III. ARBITRATION IS NOT A FAVORABLE FORUM FOR CONSUMERS TO CHALLENGE ILLEGAL CONTRACTS.

A. The Rules that Govern Binding Mandatory Arbitration Are Skewed in Ways that Impede Consumer Challenges.

In addition to the cost and efficiency concerns raised above, arbitration is generally *not* a favorable forum for consumers to challenge the illegality of a contract. In its brief, FiSCA suggests that the threat of unconscionability or other challenges ensures that mandatory arbitration clauses and procedures are fair. (FiSCA Br. 14-15.) What FiSCA generously characterizes as "[m]eticulous efforts to assure fairness" (*id.* at 14) appear instead to be painstaking attempts to draft clauses that favor corporate entities as much as possible but narrowly evade judicial invalidation. The number of arbitration clauses that have successfully been challenged as unconscionable is hardly proof that the remaining clauses are fair or consumer-friendly.[6]

Quite the contrary, the rules that govern binding mandatory arbitration are often skewed in ways that make it very difficult for consumers to challenge an illegal contract. The limits that binding mandatory arbitration frequently places on discovery and on the evidence that may be introduced naturally disadvantage consumers, who may need to establish a

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tion clause "effectively meaningless" is without merit. (American Bankers Association Br. 16.) In fact, arbitration parties frequently have to resort to the courts because of the arbitrator's limited powers. For example, a party to arbitration may need to file a court action to compel a third-party witness to attend or to confirm an arbitration award. *See* 9 U.S.C. §§ 7, 9.

[6] One of the sources cited by the Chamber of Commerce found that courts struck down over 80 arbitration contracts as unconscionable in 2002 and 2003. Susan Randall, *Judicial Attitudes Toward Arbitration and the Resurgence of Unconscionability*, 52 Buff. L. Rev. 185, 194 (2004), *cited in* Chamber of Commerce Br. 15 n.15.

pattern or practice or make a similar showing to prove their claims. Access to discovery is especially important for consumers in disputes with financial institutions because "the institution or third parties have within their exclusive possession the critical information and documents the consumer needs to prove the case." Mark E. Budnitz, *Arbitration of Disputes Between Consumers and Financial Institutions: A Serious Threat to Consumer Protection*, 10 Ohio St. J. on Disp. Resol. 267, 283-84 (1995). The secrecy surrounding arbitrations also disfavors consumers by concealing evidence, findings, and legal conclusions that might inform other victims of their rights or assist them in developing their claims. *See, e.g., Ting v. AT&T*, 319 F.3d 1126, 1152 (9th Cir.), *cert. denied*, 540 U.S. 811 (2003).[7]

Companies frequently draft arbitration clauses to limit or prevent certain types of traditional monetary damages that predominantly benefit consumers and are central to effective law enforcement, including punitive damages and certain types of compensatory damages. *See* Budnitz, *The High Cost of Mandatory Consumer Arbitration*, *supra*, at 137, 141 & n.50.[8] Arbitration clauses may also include other one-sided provisions that benefit only companies, not consumers—for example, excluding from coverage certain types of claims that only companies would bring. *See, e.g.*, NAF, Drafting Mediation and Arbitration Clauses: Practical Tips and Sample

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[7] Contrary to FiSCA's assertion that "[r]ational litigants would shun the invocation of the [Federal Arbitration Act] when it would entail the disclosure of unseemly practices" (FiSCA Br. 14 n.9), the arbitral forum is *precisely* where a party engaged in illegal activity would want claims against it to be heard.

[8] Punitive damages are designed to deter both the company that is a party and other businesses from engaging in illegal conduct. Together with the secrecy of arbitration proceedings, the absence of punitive damages can make it not only feasible, but even profitable, for companies to write off what few losses they might have in arbitration as a cost of doing business, without altering their practices.

Language 11 (2005), *available at* http://www.arb-forum.com/resources/white_papers/05clauses.pdf (providing language for a mortgage agreement arbitration clause that would preserve the right to proceed in court to exercise "all rights to foreclose against any real or personal property or other security by exercising a power of sale granted under Loan Documents or under applicable law or by judicial foreclosure and sale, including a proceeding to confirm the sale"); *Little v. Auto Stiegler, Inc.*, 63 P.3d 979, 983-85 (Cal.) (discussing an "unconscionably one-sided" arbitral appeal provision in an employer-mandated arbitration clause that only permitted appeals of awards that exceeded $50,000), *cert. denied*, 540 U.S. 818 (2003). As noted above, prohibitions on class actions also prevent many consumers from filing at all, particularly in cases where each individual's stake may be relatively small.

In addition to industry-favoring rules, companies may benefit from a repeat player effect in consumer arbitrations because they may be involved in hundreds, thousands, or even tens of thousands of arbitrations, while each consumer claimant will likely participate in only one. *See generally Ting*, 319 F.3d at 1152 (noting the "advantages [for AT&T] inherent in being a repeat player"); *Cole v. Burns Int'l Sec. Servs.*, 105 F.3d 1465, 1476 (D.C. Cir. 1997) (discussing the advantage that an employer gains as a repeat player in cases involving mandatory arbitration of individual statutory claims); Lisa B. Bingham, *Employment Arbitration: The Repeat Player Effect*, 1 Emp. Rts. & Emp. Pol'y J. 189, 206, 213 (1997) (finding a repeat player effect in a study of data from 270 AAA arbitration cases decided in 1993 and 1994 under rules then in effect). First USA, N.A. is an example of a repeat player. Between 1998 and 2000, it filed over 51,000 claims against cardmembers with NAF. Caroline E. Mayer, *Win Some, Lose Rarely?: Arbitration Forum's Rulings Called One-Sided*, Wash. Post, Mar. 1, 2000, at E1. The cardmember prevailed in just 87 of the 19,705 awards made by

the year 2000, while First USA prevailed in 19,618 or over 99.5%. *Id.* Arbitration providers and arbitrators also may have an economic interest in being selected by companies for future cases. *See, e.g., Mercuro v. Superior Court*, 116 Cal. Rptr. 2d 671, 678-79 (Ct. App. 2002) ("The fact an employer repeatedly appears before the same group of arbitrators conveys distinct advantages over the individual employee. These advantages include knowledge of the arbitrators' temperaments, procedural preferences, styles and the like and the arbitrators' cultivation of further business by taking a 'split the difference' approach to damages."); Jean R. Sternlight, *Panacea or Corporate Tool?: Debunking the Supreme Court's Preference for Binding Arbitration*, 74 Wash. U. L.Q. 637, 685 (1996) ("[A]rbitrators may be consciously or unconsciously influenced by the fact that the company, rather than the consumer, is a potential source of repeat business."). These considerations combine to make it very difficult for consumers to challenge illegal contracts in binding mandatory arbitration proceedings.

B. The Ernst & Young Study Does Not Prove that Arbitration Results Favor Consumers.

Due to the secrecy surrounding arbitral proceedings, consumer advocates and academics have had great difficulty gaining access to arbitration data to conduct studies. Although a California law enacted in 2002 requires public disclosure of certain arbitration information, some companies, including NAF, have failed to comply fully. *See* Cal. Civ. Proc. Code § 1281.96; *Klussman v. Cross-Country Bank*, No. 2001-026688, slip op. at 9 (Cal. Super. Ct. Oct. 28, 2004) ("By way of dicta, the Court notes that the arbitration provision may also be unenforceable because NAF does not comply with C.C.P. 1281.96."); California Dispute Resolution Institute, *supra*, at 27-32. Rather than facilitating truly independent research, industry groups have commissioned their own studies. For example, Wilmer Cutler Pickering

Hale and Dorr LLP engaged Ernst & Young LLP to conduct a study with financial support from the American Bankers Association and the participation of NAF. Ernst & Young LLP, Outcomes of Arbitration: An Empirical Study of Consumer Lending Cases 2, 19 (2004), *available at* http://www.arb-forum.com/media/EY_2005.pdf. The American Bankers Association, CFSA, and FiSCA all tout this study in their briefs for the proposition that consumers prevail more often than companies in credit-related arbitration proceedings and that consumers are satisfied with the arbitration process. (American Bankers Association Br. 15-16; CFSA Br. 10; FiSCA Br. 16-17.) On closer examination, however, it is clear that the study does not prove either proposition.

The Ernst & Young study only addresses the arbitral claims that consumers actually filed and fails to consider all of the claims that were *not* filed because of the barriers that consumers face when considering whether to pursue an arbitration claim. In gauging the volume of claims that consumers forego each year, it is telling to compare the number of claims filed by consumers with the number filed by companies *against* consumers. As of the year 2000, First USA had filed over 51,000 NAF claims against cardmembers, while only *four* cardmembers had filed arbitration claims with NAF against First USA. Mayer, *supra*, at E1. Similarly, although NAF administers over 50,000 arbitrations each year, it had only 226 consumer-initiated files for the four-year period from January 2000 to January 2004. NAF, Drafting Mediation and Arbitration Clauses, *supra*, at 15; Ernst & Young, *supra*, at 7.

In light of all the factors that might dissuade consumers from filing arbitration claims and the incredibly small percentage of consumers who proceed to arbitration, one would naturally expect consumers who *do* pursue arbitration claims to have especially strong claims and to prevail in a very high percentage of cases. Even if the Ernst & Young study could

establish that consumers prevail in more than half of the arbitration claims they file, such a showing would not prove that arbitration favors consumers *overall* since many consumers who might have litigated viable claims may be dissuaded from filing an arbitration claim at all.

Moreover, the Ernst & Young study does not prove that consumers in fact prevail more often than businesses in consumer-initiated, credit-related arbitration claims. Ernst & Young used two different flawed measures to determine how many consumers had prevailed. *See* Ernst & Young, *supra*, at 9-10. Under one measure, Ernst & Young treated 117 claims—more than half of the 226 claims studied—as ones in which the consumer prevailed simply because the claims were dismissed at the claimant's request. *Id.* at 9 & n.11, 23. Far from prevailing, many of these consumers likely abandoned their claims due to the high costs, lack of discovery, and other obstacles they faced during the arbitral process.[9] In its other measure, Ernst & Young considered only those claims that proceeded to an arbitration judgment, reducing an already small sample to just 97 claims. *Id.* at 10. Under both measures that it used, Ernst & Young categorized *any* damage award as a case in which the consumer prevailed, without regard to the relative sizes of the individual's claim and the award. *Id.* at 9 n.11. The problem with this approach is obvious: A consumer who seeks $1,000 in damages from a company and obtains only $50 in relief has not prevailed. Because of the flaws in both of the measures that Ernst &

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[9] Of 118 files that were dismissed at the claimant's request, Ernst & Young treated only one as one in which the consumer did not prevail, and in that case did so only because the file explicitly stated that the consumer could not afford to continue. Ernst & Young, *supra*, at 9 & n.11, 23. Ernst & Young acknowledged that its reviewers had to "use their judgment" to determine whether consumers had prevailed in certain cases. *Id.* at 9 n.11. It also admitted that it did not compare its results to the results that consumers obtain in comparable court cases. *Id.* at 6.

Young used to determine who prevailed, *amici curiae*'s assertions that consumers have prevailed in 55% or "close to 80%" of consumer-initiated, credit-related arbitrations are not supported by the study. (American Bankers Association Br. 15-16; CFSA Br. 10; FiSCA Br. 17.)

The Ernst & Young customer satisfaction phone survey also cannot bear the weight that the American Bankers Association, CFSA, and FiSCA place upon it. NAF representatives made the initial contact with each consumer during the survey calls, a fact that likely discouraged people who had negative experiences from participating or responding candidly. *See* Ernst & Young, *supra*, at 19. Additionally, the survey results are based on just 29 responses. *Id.* at 7 & n.9. Phone surveys can introduce an element of bias because phones are not distributed evenly throughout society, and those who cannot be reached by phone may well respond differently than those who can. *See* U.S. Dep't of Commerce, Falling Through the Net: Defining the Digital Divide, at pt. IB (1999), *available at* http://www.ntia.doc.gov/ntiahome/fttn99/contents.html (noting disparities among different demographic groups regarding telephone penetration); Owen T. Thornberry & James T. Massey, *Trends in United States Telephone Coverage Across Time and Subgroups, in Telephone Survey Methodology* (Robert M. Groves et al. eds., Wiley & Sons 1988). This selection bias is of particular concern in the Ernst & Young study because NAF lacked current contact information for 71 consumers, did not reach 64 other consumers, and spoke with 11 consumers who refused to participate in the survey. *See* Ernst & Young, *supra*, at 7 n.9, 11, 18. Given all of the deficiencies in the Ernst & Young study, there is no reason to believe that the 29 people who responded were in any way representative of all consumer arbitration claimants.

IV. POST-ARBITRATION JUDICIAL REVIEW AND PUBLIC ENFORCEMENT AUTHORITY DO NOT OBVIATE THE NEED FOR COURTS TO DETERMINE THE LEGALITY OF CONTRACTS BEFORE ARBITRATION.

A. Vacating an Arbitral Decision Is Very Difficult Under Current Law.

Acknowledging the possibility that an arbitrator could enforce an illegal contract, the petitioner asserts that "[i]f the arbitrators were to exceed their authority, or otherwise manifestly disregard the law, then a court could always vacate their decision." (Pet'r's Br. 18.) This statement fails to acknowledge how difficult it is under current law to vacate an arbitral decision. *See, e.g., Brabham v. A.G. Edwards & Sons Inc.*, 376 F.3d 377, 380 (5th Cir. 2004) (stating that the court's review of an arbitral award is "exceedingly deferential" and that it could "permit vacatur of an arbitration award only on very narrow grounds"); *Duferco Int'l Steel Trading v. T. Klaveness Shipping A/S*, 333 F.3d 383, 389 (2d Cir. 2003) (stating that review under the doctrine of manifest disregard "is highly deferential to the arbitral award and obtaining judicial relief for arbitrators' manifest disregard of the law is rare").

While 9 U.S.C. § 10(a)(4) permits U.S. courts to vacate an arbitral award "where the arbitrators exceeded their powers," a number of courts have held that this section does not permit review of the correctness of the arbitrator's decision. *See, e.g., DiRussa v. Dean Witter Reynolds Inc.*, 121 F.3d 818, 824 (2d. Cir. 1997) ("Our inquiry under § 10(a)(4) . . . focuses on whether the arbitrators had the power, based on the parties' submissions or the arbitration agreement, to reach a certain issue, not whether the arbitrators correctly decided that issue."). Some courts have also held that the fact that an arbitrator made erroneous legal determinations is an insufficient basis to overturn an arbitral award for manifest disre-

gard of the law. *See, e.g., IDS Life Ins. Co. v. Royal Alliance Assocs., Inc.*, 266 F.3d 645, 650 (7th Cir. 2001) ("[N]either error nor clear error nor even gross error is a ground for vacating an award."); *Montes v. Shearson Lehman Bros.*, 128 F.3d 1456, 1461 (11th Cir. 1997) ("An arbitration board that incorrectly interprets the law has not manifestly disregarded it. It has simply made a legal mistake."); *cf. Moncharsch v. Heily & Blase*, 832 P.2d 899, 904 (Cal. 1992) ("[I]t is the general rule that, with narrow exceptions, an arbitrator's decision cannot be reviewed for errors of fact or law.").

Some courts of appeals have applied a standard that is extraordinarily difficult to surmount before vacating an award for manifest disregard of the law: they require proof that the arbitrator knew the relevant law yet chose not to apply it. *See, e.g., Duferco Int'l Steel Trading*, 333 F.3d at 389 ("A party seeking vacatur bears the burden of proving that the arbitrators were fully aware of the existence of a clearly defined governing legal principle, but refused to apply it, in effect, ignoring it."); *Montes*, 128 F.3d at 1461. This standard is even more difficult to meet because many arbitrators do not produce findings of fact or conclusions of law or state their reasoning. The extreme deference given to arbitrators' decisions means that post-arbitration judicial review is not a cure for arbitrators' misinterpretations of the law. Accordingly, it is critical that parties be permitted to challenge the legality of a contract that contains an arbitration provision *before* claims are arbitrated.

B. Public Enforcement Authority Alone Will Not Ensure Effective Enforcement of Consumer Protection Laws.

FiSCA asserts that "[t]he result of a decision in a simple dispute between private parties hardly can be said to imperil statewide substantive law" and argues that police powers can cure any wrongs resulting from arbitrators' enforcement of illegal contracts. (FiSCA Br. 11-12, 18-20.) These argu-

ments overlook the central role that Congress and state legislatures intended private parties to play in developing and enforcing consumer protection law.

It is well recognized that Congress intended the Truth in Lending Act, 15 U.S.C. § 1601 *et seq.*, and a number of other consumer protection statutes to be enforced by private litigants. *See, e.g., Postow v. OBA Fed. Sav. & Loan Ass'n*, 627 F.2d 1370, 1387 (D.C. Cir. 1980) (noting that the Truth in Lending Act was "specifically designed by Congress to be enforced through private citizen suits"). Likewise, in enacting state consumer protection laws, state legislatures have created private rights of action with the expectation that consumer suits would assist in developing and enforcing the law. *See, e.g., Presidential Leasing, Inc. v. Krout*, 896 So. 2d 938, 941-42 (Fla. Dist. Ct. App. 2005) (declining to enforce an arbitration clause found to be an "evisceration of the consumer legislation" because the clause frustrated the purposes behind the prevailing party attorney fee provision of the Florida Deceptive and Unfair Trade Practices Act and discouraged the individual enforcement actions the act was intended to facilitate); *Equitable Life Leasing Corp. v. Abbick*, 757 P.2d 304, 307 (Kan. 1988) (quoting Kansas statutory comment that states that the Kansas legislature provided for civil penalties under the Kansas Consumer Protection Act "to encourage enforcement of the act by a consumer acting as his own 'private attorney general'"). This private enforcement through the courts is absolutely critical to complement efforts by state and federal authorities, which simply do not have the resources that would be necessary to pursue all illegal consumer contracts or even a sizeable fraction thereof. Moreover, diverting all challenges to the legality of contracts to the "black box" that is arbitration would undermine government enforcement efforts by depriving agencies of important information as to which companies' practices are generating a common pattern of consumer complaints.

Because of the real-world limitations on public resources and all of the problems with binding mandatory arbitration discussed above, preventing consumers from challenging illegal contracts in court would impede the enforcement of important state and federal consumer protection laws.

CONCLUSION

For the foregoing reasons, the judgment of the Florida Supreme Court should be affirmed.

Respectfully submitted,

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